



Enhanced Small and Medium Sized Enterprise Development Program

Quarterly Performance Report

July 1, 2005 to September 30, 2005

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1. Background

The Enhanced SME Development (ESD) Program, funded by the U.S. Agency for International Development (USAID), is a three-year program to strengthen the development of small- and medium-sized enterprises (SMEs) in the Russian Far East by improving the regulatory environment, access to credit, and advanced and sector-specific business skills training. ESD is implemented by Winrock International, Counterpart International, and a variety of local partners including Counterpart Enterprise Fund, the Center for Investment and Support (Prognoz), the Sakhalin Association of Business People and numerous other Russian organizations. Project activities focus in the target regions of Amur, the Republic of Buryatia, Sakhalin Island, Primorski Krai, Chita Oblast, the Republic of Sakha, and Khabarovski Krai.

ESD aims to promote SME growth throughout the Far East and target under-served regions in particular. Most of the program's activities are done by or in collaboration with business services providers located in the regions through fee-for-service arrangements. Training and technical assistance are provided primarily by qualified Russian experts.

The Winrock Consortium employs cross-cutting strategies that have proved effective across different SME sectors. These strategies will be applied in all of ESD's components:

- Building business association effectiveness and sustainability
- Conducting market analysis as the foundation for technical assistance and training
- Providing demand-driven assistance, primarily through Russian experts
- Employing gender and social analysis

The project began August 1, 2003, and will continue until August 3, 2006. This report covers activities and results for the period from July 1 to September 30, 2005.

Project Administration

In addition to its partners, Prognoz (Blagoveschensk), Makon (Ulan-Ude), Business School (Yakutsk), Far Eastern Center for Economic Development (Vladivostok), and Sakhalin Association of Business People (Yuzhno-Sakhalinsk) and Counterpart Enterprise Fund, Winrock International signed a Memorandum of Understanding with the Russian American Education Center (RAEC) in Khabarovsk. Winrock has provided for a full-time training manager, Antonina Pronina, to put together ESD trainings, and RAEC will cover for all associated administrative costs, plus travel expenses for trainers, if needed.

CEF would like to continue to develop and position itself as an advanced practicing microfinance support institution and a training center in the RFE and will work to receive a microfinance rating by a microfinance rating agency. ESD will gradually concentrate on CEF's institutional development. To achieve this goal CEF plans to continue working in partnership with the Russian Microfinance Center and Counterpart International.

2. Progress Indicators

2.1. Improving Regulatory Environment

Counterpart approaches regulatory reform by means of working with local associations as much as possible. Upon the conclusion of the ESD program, Counterpart will have left a legacy of local organizations that can effectively advocate for entrepreneurial rights. Two important areas of change involve reducing the number of inspections to the number allowed by law and ensuring that new business registration proceeds according to law.

In general, business associations in the RFE are weak and for the first two years of the project, Counterpart provided organizational development training focused on each association's needs. As they became stronger, the project introduced advocacy training such as "Carrying Out Advocacy Actions and Campaigns" and "Effective Collaboration Between Authorities and Associations." Once they had completed this training, Counterpart began mentoring the associations and providing grants to develop and conduct advocacy campaigns and, thus, gain experience.

For Year Three, Counterpart is undertaking the regulatory reform component, primarily through a grant mechanism, and helping the associations institutionalize what they have learned by continuing to conduct advocacy campaigns. If any of the associations require financial resources, the project will help them apply for ESD advocacy grants.

In addition, Counterpart is facilitating development of business association networks and coalitions to achieve common goals. Bringing association leaders together periodically to share information, best practices, and lessons learned and to identify potential areas for collaboration on advocacy issues is helping to build working relationships and make the associations and networks a strong force for change.

Monitoring Results

Prognoz. In July, Prognoz finished its analysis of questionnaires collected from SMEs operating for less than one year to gauge progress in decreasing the amount of time it takes to register an SME. Staff also analyzed questionnaires received from enterprises operating for more than one year to determine the degree of reduction in the number of inspections conducted. To ensure a reliable measure of progress, Prognoz questioned the same businesses they had previously polled.

The study concluded that for SMEs operating more than one year, the inspection burden had decreased with only three agencies continuing to conduct unscheduled inspections—tax, fire protection, and sanitary. The survey also found that the transparency of Labor Protection and Police Department inspections had increased significantly.

SABP – Monitoring results also showed positive changes in Sakhalin region. SABP reported that 76% of inspections carried out in Sakhalin were scheduled, a 14% reduction in the number of

unscheduled inspections (baseline December 2003). The number of inspections conducted by specific agencies also decreased—tax inspections by 6.5%, fire department inspections by 6.3%, labor safety inspections by 8%, and militia inspections by 6%. These results demonstrate that entrepreneurs are having fewer problems with certification authorities. Most survey respondents believe that since December 2003 the inspection process has become clearer and more predictable.

At the same time the surveys highlighted the problems on which BAs should concentrate. For example, introduction of imputed earnings tax, bidding process transparency for municipal orders, violation of healthy competition law, conducting of unscheduled inspections, land renting issues, etc.

Overcoming Administration Barriers through Advocacy Grants

Taking into consideration increased capacity and strength of supported Bas, Counterpart made important changes to the grants manual, expanding the list organizations eligible to apply for grants from BAs to other NGOs and groups partnering with BAs or NGOs. In addition, the maximum amount was increased to \$5,000 and the project period expanded to six months. Counterpart also encourages applicants to work together through coalitions or networks to solve local problems.

To inform business, government, and public society about the expanded opportunities available through advocacy grant programs, ESD and its partners conducted ***three information workshops*** for potential grant recipients in which attendees learned about ESD program operations in Sakhalin Oblast, Amur region and Buryatia. They discussed in detail the grant component objectives and tasks, the procedures for applying for grants, how to develop a project budget, and financial reporting requirements. Partners also distributed information about grants at various meetings, conferences, and roundtables conducted by the BAs.

Advocacy Grants

From February through April, the **business association in Nevelsk** implemented an advocacy microgrant aimed at overcoming administrative barriers to obtaining a legal trading license. SMEs in Sakhalin had to fulfill three requirements to get such a license and this contradicted a local law specifying requirements for acquiring a license and prohibiting requests for documents not included on the list. These additional requirements created barriers for SMEs trying to do business in Sakhalin and the association published an article in the local newspaper entitled "Barriers for Businessmen" that described the problem and its consequences in order to raise the awareness of key stakeholders. The association then held a roundtable with Nevelsk authorities and entrepreneurs to protest the additional barriers and request alignment of Nevelsk Region legislation with that of Sakhalin Region. This resulted in more than 140 entrepreneurs of Nevelsk region becoming eligible to obtain a legal trading license.

From March through May, the **Entrepreneurs Union of Aniva Region** initiated an advocacy microgrant project "Optimizing Small Business Support Fund in Aniva Region" aimed at eliminating administrative barriers and enhancing transparency of the SME Support Program. This government program was designed to support SMEs financially, but entrepreneurs were dissatisfied with the activity because the municipality allocated money without consulting

businesspeople or publicizing information on loans to encourage competition. The fund lacked transparency and was a violation of the mayor's provision. The ESD microgrant familiarized the business community and Duma with the Fund's performance and developed rules and procedures for loans to encourage SME development. The Union submitted the documents to the Mayor's Office.

Another result of the grant was creation of a Public Council comprising 17 members, to serve as an advisory body of entrepreneurs, officials, public representatives, and external experts to discuss law drafts, government regulations, etc. prior to submission to the Duma. During its first session, the Council considered proposals and documents developed within the framework of the grant and forwarded them to the Mayor of Anivsk District with a recommendation to speed up the decision-making process on proposals, particularly the one focused on Fund operation.

Uglegorsk Entrepreneur's Union implemented an advocacy grant from June through August to deal with changes to the RF Tax Code initiated in January 1, 2005. The changes concerned imputed earnings tax and gave municipalities the right to determine this tax locally. Following these changes, entrepreneurs in Sakhalin had to pay an imputed earnings tax of more than two and half times the previous amount. When many entrepreneurs became almost bankrupt the entire region suffered.

The grant project "Improving Tax Legislation" was implemented jointly by the **Uglegorsk Association of Entrepreneurs** and BAs in three other regions. They developed proposals to decrease the adjusting factor for the calculation of the imputed earnings tax and to make amendments in the Sakhalin Oblast Law. These proposals have been submitted to the Sakhalin Regional Duma Economic Policy and Budget Committee and were considered by the Legislative body in September. Based on the deputies' decision they were submitted for examination by the Sakhalin Oblast Revenue, which recommended that municipalities adopt these proposals no later than October 2005. An additional benefit provided by the grant project was this consideration of proposals by the Sakhalin Oblast Revenue.

Poronaisk Central Library received a grant to decrease the load and stress on business activities executed by the controlling units in the Poronaysk District and to improve the legal literacy of small businesses when interacting with controlling units by providing information support and organizing information seminars. To make the grant activities more effective, the grantee is cooperating with the Poronaysk District Association of Business People.

Also during the quarter, the ESD office received *three new grant applications* sent them to the Grant Committee for consideration.

Partner Collaboration

On September 22, 2005, the Chairperson of SABP Tatiana Garshenina and the Prognost Center in Blagoveshchensk conducted a focus-group session on problems facing SMEs in order to identify potential grantees and grant project topics. They also discussed problems in the Amur Oblast, which continue to hinder SME development. These include unsanctioned inspections carried out by controlling units, inactivity of local authorities regarding problems facing SMEs, administrative constraints imposed by local authorities, frequently changing federal legislation

and imperfection of local laws, the lack of legal knowledge among businesspeople, red-tape and procrastination of officials in solving business issues, the lack of a documents regulating land development in Amur Oblast, and the deficiency or inefficiency of mechanisms and tools for interaction between business and local authorities.

2.2 Improving Access to Credit

Counterpart's approach to increasing SME access to credit and leasing is to work with both borrowers and lenders. Although we engage in many kinds of activities to achieve results, our main input is training for financial institutions in working with collateral and how to utilize nontraditional forms of collateral when dealing with SMEs; creating new financial products for SMEs; and Bank-MFI cooperation as a means of lending to SMEs. The training was very successful during the first two years of the project and goals for access to credit and leasing facilities were met.

Loans

During this quarter, SMEs received 459 loans worth \$2,273,353 from participating banks and non-bank financial institutions and signed 10 leasing agreements worth \$198,235. This is a direct result of the training sessions that Counterpart and CEF provided these institutions over the life of project.

Table 1 - Breakdown of loans and leases by type of financial institution

Financial Institutions Reporting	Total Loans	Loans to Women	Amount of Loans
SME Support Funds	13	10	\$86,807
Credit Cooperatives	289	198	\$910,456
Banks	157	36	\$1,276,090
Leasing Companies	10	2	\$198,235

In April, ESD partner **Business School** organized and conducted a roundtable for banks and MFOs in Yakutia “Collaboration between Banks and Microfinance Organizations in Dealing with SMEs”. Facilitators provided examples of successful bank/mfo cooperation and twenty-five participants discussed how Yakutia banks and MFOs could work together. This resulted in the Yakutsk branch of Sberbank signing an agreement with two credit cooperatives and ESD partner Business School to exchange information on mutual interest, participate in staff trainings and seminars, and develop techniques for serving their SME clients.

In the third quarter, Counterpart's primary partner, CEF, decided that it wanted to gradually concentrate on its own institutional development and to position itself as an advanced practicing microfinance institution and a resource center in the RFE. CEF is constantly developing new products and services for its clients and it also is an experienced consulting firm with several clients, including non-bank financial institutions such as the Kamchatka Fund for SMEs Support “Sodruzhestvo”, the Blagoveschensk Fund of Economic and Social Development, and the Autonomous Nonprofit Organization – Credit Union Development Center in Vladivostok.

During the second year of the ESD program, CEF developed training modules for banks on SME lending and establishing cash-flow needs for SMEs. CEF employees participated in two ‘training of trainer’ (TOT) sessions with the Russian Microfinance Center and the St. Petersburg Foundation for SME Development. Working in partnership with the Russian Microfinance Center in the framework of ESD, CEF plans to further develop microfinance trainings and consulting for non-bank financial institutions in the RFE.

Training model development

In September CEF developed a TOR for a training module entitled “Fundraising for Non-Bank Financial Institutions.” Lack of loan capital is a problem for non-bank financial institutions and thus it is a barrier to SME lending. To help overcome this, CEF developed a TOR for a new training module on the topic of fundraising so that they have more capital with which to lend to SMEs. CEF identified a consultant able to work on this model and expects the product to be ready in early November. The model will be based on CEF's own experience and once developed, CEF will organize seminars and consultations for local credit cooperatives and funds for small business support to pilot the training.

Rating Evaluation for the Counterpart Enterprise Fund

To fund the planned expansion of its lending activities to other areas of the Russian Far East (i.e., portfolio growth), CEF is looking for serious foreign commercial investors like the International Financial Corporation, Blue Orchard Finance S.A., Deutsche Bank Microcredit Development Fund, etc. In order to attract serious foreign investors, CEF needs a rating to prove its creditworthiness. Being a leading MFI in the Russian Far East, CEF also wants to be the first to obtain a rating from an International MFI Rating Agency and it plans to share its experience and the process of obtaining a rating with other MFIs of the region.

To contract a MFI Rating Agency to provide a rating evaluation of CEF, the organization developed a TOR outlining the scope of rating evaluation services to be delivered by the MFI Rating Agency to CEF. ESD managers have contacted rating agencies with experience working in Russia.

2.3 Advanced Business and Sector-Specific Training

This quarter Winrock continued to work with its **six** major training partners and other regional training centers to expand availability of advanced and sector-specific training in Russia Far East. **24** training courses for **391** entrepreneurs were offered in all targeted regions in April-June 2005:

Table 2 - Type of Trainings by Region and Number of participants

Region	Trainings			Participants		
	Adv.Bus	SSpecific	Total	Adv.Bus	SSpecific	Total
Amur Oblast	4	1	5	64	13	77
Buryatia	6		6	71		71
Khabarovsk Krai	6		6	127		127

Primorye	4		4	77		77
Sakha (Yakutia)	3		3	39		39
TOTAL	23	1	24	378	13	391

2.3.1 Advanced Business Skills Trainings Conducted

During January-March 2005, ESD supported its partners in providing **23** demand-driven advanced business skills training courses in the targeted regions for **378** entrepreneurs.

As the ESD program closes in 2006, our goal is to leave behind sustainable institutions that will be able to continue providing training and consulting services to RFE SMEs. To achieve this goal, ESD focuses on partners' institutional development, and encourage use of local trainers and training modules developed by the program.

Training modules

During the reported quarter, the following modules were developed and placed on the ESD web site:

- 1) *Renovation of Company's Fixed Assets*, by Maria Frolova (Khabarovsk)
- 2) *Use of Information Systems in Management of Small Enterprises*, by Danila Belousov (Blagoveschensk)
- 3) *Development of Ecotourism in the RFE*, by Larissa Kurbanova (Khabarovsk)

Each module contains theoretical and practical material, case studies, samples of hand-outs for participants and recommendations to trainers on how to use the module. Three of these modules have been already used by Partners' organizations for conducting trainings.

Use of local trainers

ESD partners have significantly increased the use of local trainers, giving them the opportunity to get known in the region and promote their services. Out of **24** trainings conducted in the RFE last quarter, **20** have been conducted by trainers from the region.

Distance Learning

ESD partners have been distributing distance learning courses on CDs, developed by the program. Two training courses have been published entitled *Merchandising*, and *Effective Sales Techniques* by Roman Simutkin. **Ninety** entrepreneurs have been trained through this course in July-September 2005.

2.3.2 Sector-Specific Trainings Conducted

July 21-22, a Blagoveschensk trainer Larissa Simutina conducted training for **13** construction companies on how to reduce companies' costs. Participants learned about specifics of financing in construction businesses, managing personnel, saving resources, and cost distribution between the key accounts. Center Prognoz, the organizer of this training, was later invited by construction companies to participate at the citizens' forum on the housing reform in Amur Oblast.

Consulting sessions conducted in the previous periods, have started to bring results, for example:

ESD Program Helps to Introduce the Budgeting System for WOODEX Co.

The General Director and Financial Director of Woodex, a medium-sized company that supplies building and finishing materials for the Russian Far East markets attended several trainings provided by ESD including the *Accounting Management and Budgeting* training and a series of consulting sessions provided by experts A. Kochemasova and Ye. Shinkorenko from Khabarovsk.. They learned about determination and responsibility centers, use of transferred prices; budget formulation; budget reconciliation, etc and applied these principles to their company. The budgeting system enables Woodex to plan its activities more accurately, cutting expenses by 9% and increasing profit margins by 15% for September 2005.

2.4 Sector-Specific Consultancies

As part of the strategy for sustainability, the ESD Program is supporting our partners with technical assistance. ESD partner organizations would like to develop themselves as consulting centers. Five ESD partner organizations at the Partners' Meeting in May 2005 requested from ESD the training on how to develop consulting services at their organizations. During the reported period Makon, Prognoz, FECED, Business School and SABP have identified possible consulting opportunities to be later fulfilled by their staff. At the ESD training in October, they will have a chance to discuss these projects with trainers and colleagues to find the best possible solutions to companies' problems.

2.5 ESD Program Impact

ESD partners report the program's success through monitoring the impact that the program activities make on the business environment of their regions.

2.5.1 Impact from Business and Sector Trainings

ESD partner FECED has developed a questionnaire to measure the program impact on the companies that have been trained under ESD. The questionnaire assess whether the general impact from trainings is positive and useful, whether the enterprise's client base and sales have increased as a result of acquiring new skills and knowledge at ESD trainings. The results of the questioning are presented in the following table:

Table 3 Results of the Impact Questionnaire

Regions	Number of Respondents	Positive General Impact on Companies %	Increase of Clients Base for Companies %	Increase of Sales for Companies %
Khabarovsk Region	25	100	100	100
Primorsky Region	54	72	81	74
Sakha (Yakutia)	31	100	94	97
Buryatia	46	87	72	56
Amur Oblast	52	88	63	72

In addition, companies commented that short-term business education had the following effect on their operations:

- Quality of services has increased, sales people have become more client-oriented
- Company managers now understand the importance of self-development and training for staff
- Trainings have promoted understanding between managers and other personnel
- New businesses have been opened and new jobs created

Here are some examples of the ESD **sector trainings** on the business development in the regions:

Restaurants Run by Women Are Rapidly Developing in Buryatia

A majority of restaurants in Buryatia are owned and run by women. Many of them have attended trainings and seminars, and received consultations provided by Center “Makon” specialists. Such trainings and seminars became possible due to the technical assistance provided by the ESD Program. During last year, all these enterprises increased their profits by 10% to 30% and the number of customers by 20% to 50%. In addition, coffee house “Zolotaya” obtained a credit for expanding its business. Restaurant “Stolitsa” won the first place in the contest among the restaurants of Buryatia, which was organized by the Buryat Association of Restaurateurs. Café “Titan-Kvartal” got a credit in the amount of 3 million Rubles (\$100,000) for building “Mega-Titan” Complex. All these facts prove that businesses run by women are not stagnating, but rather rapidly developing, propped up by the ESD Program. These vibrant businesses generate more profit and reinvest it into their future development.

The Versailles Hotel Increases Number of Guests and Generates More Profits Due to ESD Program

In September 2004, Erik Erlandsen, an ESD Program volunteer from the USA, consulted Mrs. Timofeyeva, the General Manager of the Versailles Hotel. Mr. Erlandsen suggested that the Versailles Hotel should position itself as a business-hotel, that is, a hotel servicing first of all business travelers and guests coming to Khabarovsk.

From September 2004 through August 2005 the Versailles Hotel followed Mr. Erlandsen’s recommendations and increased the number of services provided, created and supplied a conference hall and a business center (with a laptop?), established a stores (kiosk and gift shop) with a range of assorted goods tailored to accommodate businesspeople, advertised the hotel was advertised in bus depots, railroad stations and airports of Khabarovsk krai; developed service package contracts with airlines having their offices in Khabarovsk.

The Versailles Hotel to become more visible than its competitors and has increased the number of guests by 15 percent and profit margins by 11 percent. By February, 2006, the hotel management is planning to increase profit by 25 percent.

2.5.2 Impact from Development of Associations

One of ESD program goals is to improve the regulatory environment in the selected regions (Sakhalin, Amur region and Buryatia). We implement it by collaborating with BAs, local government authorities and public organizations. Only organizationally strong and financially

self- sustainable business associations are able to provide support to SMEs and to advocate for an improved business environment. ESD program first worked on strengthening BAs through organizational development training. Once the associations completed the organizational training, we began to provide advocacy training for them. Finally to assist the associations, ESD began issuing advocacy microgrants to assist them in their advocacy campaigns by providing necessary funding for events such as roundtables or hiring a consultant, if needed.

For example, in Sakhalin, SABP assessed targeted business associations in August 2005 and noted the following positive changes: basic management skills have improved, and associations are becoming financially sustainable through a combination of membership dues and commercial services to non-members. The association in Nevelsk increased the number of members and which resulted in a 10.5% increase in income from membership dues. With more financial resources and a larger number of members, the association has become a stronger and more powerful force that represents entrepreneurs in advocating for their rights.

The association also created and printed a brochure explaining its work in order to attract more new members. The image of the association in Ulegorsk has significantly improved over the past year. In June 2005, the Ulegorsk Association of Entrepreneurs carried out an advocacy campaign with the purpose of decreasing the imputed earnings tax within the ESD Program grant project. This advocacy campaign was successful. For more information see **Section 2.1**.

2.5.3 Impact from Microfinance Activities

Until recently there has been no credit for businesses in Vladivostok. In September 2004, a NGO (autonomous non-profit organization) “the Pacific Center for Credit Unions Development” was registered with one of its objectives to provide credit to businesses.

Within the ESD Program’s framework Counterpart International (CPI) provided assisted this newly created organization to prepare a business plan, to develop credit policy, to develop templates of documents, to define the terms and conditions of the credit. The Center’s employees were trained at CEF’s premises. In addition, ESD Team assisted the Center for Credit Unions Development to establish ties with banks and the Center’s employees were taught negotiating skills to help them get credit lines in the future.

As a result, the number of loans increased from 4 credits agreements totaling \$9,123 in 2004 to 20 credits totaling \$92,982 between February and September 2005. At present, the Center provides credit not only to credit cooperatives, as it used to be earlier, but also to entrepreneurs.

Owing to the ESD Program, the entrepreneurs of Vladivostok now have real opportunities to access credit.

2.6 Outreach and Communication

The ESD Chief of Party, staff and partners have been in constant communication with other international projects, such as Russian American Education Center in Khabarovsk, BISNIS, ISC, Eurasia Foundation, Russian Microfinance Center, and CIPE. We share information, resources, exchange ideas and ensure collaboration with these and other organizations.

The ESD partner organizations have become very visible in their regions. July 11, Aleksander Abramov from FECED was invited to participate at the Council on Small Business' Affairs at the Primorye Governor's office. He spoke about the ESD program and its potential to develop innovations in SMEs. Andrey Konushok from Prognost was one of the organizers of the conference "Legal Issues in Amur oblast SMEs" in September. Aitalina Sokolova from Business School presented the ESD program activities at the roundtable "Dialog between Government and Business" in Aldan (Yakutia) September 23-24.

The ESD Chief of Party and Senior Manager participated at the 10th Annual Meeting of Russian-American Pacific Partnership (RAPP) in Yuzhno-Sakhalinsk September 12-13. ESD managers participated in discussions about NGO sector status, business and operating environment in Russia and the RFE, and issues of enhancing regional and community development.

Program Coordinator Erin Hughes shared information with participants of Khabarovsk's Far Eastern Economic Congress in late September.

The ESD Program **website** continues to be updated. We publish training schedules, calendars of events, training materials and other resources on the web to ensure information exchange and collaboration between the project's partners. It provides information about the program's activities, findings and results to date.

3.1 Problems/Difficulties Anticipated in the Next Three Months

None at this time.